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muse ADVISORY

8 things to think about when setting your endgame objective

The phrases "endgame" and "journey plan" have become popular over recent years. Often these phrases only consider funding and investment, with the term "data journey" also starting to get a bit of momentum. But there's more to your endgame journey that should be considered upfront if you don't want to risk your progress becoming more costly, slowed down, or de-railed altogether, and of course to keep the member front of mind.

Here are 8 things to think about when setting your endgame objective:

1 Long term funding objective – setting out your overall direction of travel

It enables all Trustees, advisers and the sponsor to understand and align with the main purpose of the Board and what is it trying to achieve.

The long-term funding objective might be something like "To secure the Scheme's benefits with an insurance company", or "To achieve self-sufficiency and reduce reliance on the Sponsor".

A funding objective may be agreed between the Trustee and Company as part of a valuation and expressed in a form such as Gilts +0.3%. A funding objective expressed in this way may not get you completely to your final end point, whatever that is for your scheme.

2 Investment strategy

Depending on the long term funding objective and your time horizon, there may be specific investments to target, e.g. for a buy-in objective, there may be advantages in moving to an investment/ risk profile that looks similar to that of an insurer. If the scheme has Illiquid assets, early planning will allow you more flexibility to manage the sale of these assets and to maximise your ability to take opportunities when they arise, and to ensure they do not become a barrier to a transaction.

There may also be clauses in investment manager agreements that need to be understood and taken into account in your planning. For example, can the manager extend investments for a fixed period, or can they make capital calls on the scheme at a time when it is unexpected and not budgeted for?

3

Covenant reliance

Agreeing the level of reliance on the company covenant and the target timescales for any change. Consider if there is any urgency to reducing reliance on the sponsor, and what could change in the future to trigger the need for a more urgent evolution?

4

Transaction readiness

Agreeing your approach to transacting, for example, whether you wish to undertake multiple buy-ins or a whole scheme buy-in, and your intended timeframes between buy-in(s) and buy-out, will frame the duration and structure of your journey, and any potential risks and challenges you might face in both your project and the interim operations along the way.

In addition, considering Trustee protection requirements, including residual risk, run off risk or sponsor indemnity requirements, balanced against likely insurer exclusions and the sponsor's willingness to provide such indemnity, is also a useful check that a transaction remains the right path for the scheme.

5

Data and benefits

As the buy-in market becomes busier, insurers are becoming choosier with who they transact with. Those with good quality and recently tested data, and a documented benefit specification are more likely to be attractive.

With capacity constraints in the administration markets (and potential resource conflicts with other forthcoming regulatory projects, e.g. Pensions Dashboard), identifying and planning data and benefit projects early will help enable efficient use of resource, in time to meet the agreed endgame objective. Planning early also allows you to identify if there are any efficiencies to be gained by combining certain data and benefit projects, e.g. to ensure backfiles only need to be reviewed once or member benefit corrections are made once at the end of the process.

6

Member engagement and communications

Planning how to engage with members has the potential to shape how responsive members are, e.g. if collecting data is required in future. It can also influence how vocal they might be when the Trustee makes a transaction, potentially influencing any timescale to windup.

The Trustee should consider what it wants the member experience to look like from an administration point of view during the journey and following any transaction. Service level agreements (SLAs) and automation levels may be affected by a buy-in transaction and/ or at the time of buy-out, as well as in other end game strategies such as moving to consolidators.

7 Member options

Member options exercises can increase the choices available to members ahead of any buy-out transaction, after which point, the arrangements made with the insurer will determine the options and the service experience available to members.

The sponsor may also suggest exercises, as this may be a more cost-effective way to reduce liabilities than that offered by the transaction price.

8 Financial

It will be important to agree upfront, the circumstances in which the Trustee can ask the sponsor for more money. There may be a window when the sponsor can better manage the cost of a transaction on their balance sheet, and this could be factored into the strategic planning.

Consideration of how any potential or existing funding surplus is managed will also be required.

The Trustee Board and Company will be aware that the true cost of a transaction may not be known prior to the transaction taking place, with the data and benefit work within the data true-up period still to go. So understanding the Company's view on this risk and their willingness to meet any unexpected costs will be critical to a decision to proceed with a transaction.

There are many things to think about when setting your endgame objective. We have seen schemes and sponsors jointly spend significant sums of money and time to plot an endgame transaction without considering all of these areas early on, only to then uncover something that could have been identified earlier and have to put a transaction and their plans 'on hold' for an undetermined period of time.

Considering these areas early, doesn't mean your plans and priorities won't change, but it will help mitigate the chance of something you could have foreseen and managed from impacting your ability to reach your goals.

It's important the right people are included in your strategic journey planning. Often a de-risking adviser is involved, with the actuary and investment adviser sometimes involved and sometimes kept at arm's length, which brings risk if, for example, there are things in the investment manager terms that aren't brought to light early. Early conversations should also include your legal advisers, your administrator and whoever will be bringing all of the parts of your endgame plan together.

Even if you've already started your journey, there are still benefits in making sure you haven't missed anything, and everyone is aligned, heading in the same direction and moving at the same pace.

Are you considering your endgame objective?

Would you like someone to help bring it all together?

Contact Jo for practical help and independent advice at jo.fellowes@museadvisory.com